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As I see it

MOST ONE HUNDRED PERCENT MORTGAGES ARE NOW SAFE

FOR a number of years I have been urging a conservative policy on mortgage lending as I believed that many loans being made were unsound; that is, they were being made for amounts in excess of a safe percentage of the long-time value. This is in strong contrast to the policies I was advocating in the late thirties and the early forties when I constantly insisted that practically all loans were safe regardless of the amount and the terms.

The international situation, brought to a head by the war in Korea, will in my opinion result in a considerable degree of additional inflation with a corresponding cheapening of the dollar. Even if hostilities in the Far East are terminated on some fairly satisfactory basis, we have probably been sufficiently alarmed by the lack of our physical power to back up our international decisions so that for many years we will consider it necessary to devote a far larger percentage of our national income to military expenditures than seemed probable a year ago.

Money spent by the Federal government for military equipment and supplies is paid out in wages and becomes part of the purchasing power of the public. The supply of goods and services, however, available to the public is not increased by war contracts, as military supplies do not find their way into consumer markets. When the purchasing power of the public is increased without a corresponding increase of goods and services available for purchase, prices tend to rise until the money in the hands of the public is just sufficient to buy the amount of goods and services actually available.

Only if the entire expense of our Federal budget can be met from current income through taxation would there be any chance that our dollar could maintain its present purchasing power. Even though the entire cost of our increased budget were met out of current income, it still seems to me that the imposition of the tax-paying load is not likely to be such that consumer demand will be shrunk to the volume of consumer goods available.

In any tax policy in the years ahead it is certain that taxation will be increased on the upper income groups, but these increases will result primarily in a shrinkage of investment funds rather than in a shrinkage in demand for consumer goods. Only if the tax burden on the low and medium income groups is rapidly increased will it be possible to hold in line the prices of food, clothing and other mass consumption goods. With the inevitable lengthening of the work week with time and a half and double time for overtime, the average wage per hour, with or without wage freezing,

will increase. Only if taxes on the wage earner increase by an amount sufficient to reduce his expenditures in spite of his increased earnings can there be any hope of holding the line. While, of course, it is economically possible to increase taxes in this fashion, I will be greatly surprised if the Administration and Congress will have the political courage to withstand the organized and unorganized clamor that such a policy would invoke.

It seems to me that a tax which could best accomplish this purpose would be a Federal sales tax. In order to raise the necessary amount it would probably approximate 10% across the board. I can see many advantages of a tax of this sort. In the first place, it would apply to all purchases and would, therefore, be borne by people in all income groups in proportion to the amount that they bought. This would have a tendency to reduce all consumer expenditures. It should apply to all necessities as well as to luxury items, as only by applying it to all items can demand be shrunk to the point where it will equal the supply of dollars available for consumption purposes.

The second great advantage that I see in a tax of this sort is the fact that since it would be paid by everyone, everyone would be in favor of discontinuing it as soon as it was feasible. Taxes once imposed are always very difficult to remove, and this is particularly true if the weight of the particular tax in question bears more heavily on a minority group. Unless the great majority of voters feel the weight of the tax, they will probably favor its continuance with the idea that the benefits derived indirectly by them from it are greater than the cost which they pay.

It is my opinion, however, that a general Federal sales tax of this sort will not be enacted.

All government expenditures which do not bear directly on the war effort should be cut to the bone. This will probably not be done. The recent budget presented to Congress contains most of the Fair Deal measures disguised now as defense activities. We have become so accustomed to Federal hand-outs that it will be very difficult indeed for Congress to restrict many of the costly subsidies and other services being furnished by the Federal government.

It seems to me that the final result of our war activity will be that we will attempt to raise a portion of the money by heavier taxation. We will try to increase the sale of bonds to the public but, finding all of these methods unsuccessful in raising a sufficient amount, we will in the end pursue the course which we followed during World War II of selling government bonds to the banks.

It would probably be far better if we financed that portion of our debt by actually printing greenbacks. The advantages of printing greenbacks would be that the public would be alarmed and would clamor for some other policy. The inflationary effects of selling bonds to the banks are exactly the same as those achieved by the printing of money, but the public will never understand the full implications of this policy and, accordingly, will not make any effort to see that it is stopped. I believe that during the next few years the amount of money and credit in the hands of the general public available for the purchases of consumer goods will increase and that, therefore, the value of our dollar will inevitably decrease.

I think it highly probable that the deterioration of the dollar will be concealed by the same devices which are always used under similar circumstances of price and wage controls. These devices will have little permanent effect in preserving the purchasing power of our money, but they will conceal for a while the losses which it is experiencing. Wage and price controls have never worked and have been effective only in delaying the public's knowledge that the value of the money has deteriorated. We have said this constantly in bulletins published at the beginning of the Second World War. For instance, on March 13, 1941, I published an "As I See It" Bulletin headed, "The Government Can Delay But Cannot Prevent Price Rises."

How will the deterioration of the dollar affect real estate and real estate investments? The answer, I think, is rather simple. Since the dollar will be worth less, it will take more dollars to buy a piece of real estate in the future than it does at present. I am still of the opinion, however, that the value of real estate measured in units of goods and services was higher in 1946 and 1947 than it is today, and than it will probably be any time in the next few years - but real estate is not generally purchased on this basis. It is generally bought for dollars, and measured in dollars it will continue to increase in price.

I am of the opinion that 608 loans, which I have criticized so severely during the past few years as being unsound and which I still think were unsound at the time that they were made, will now pay out with relatively little loss. The deterioration of the dollar will mean that competing buildings built in the future will be built at higher cost, and this will add value to the buildings already built and will build an equity above the loan where no equity existed in the past.

It must constantly be remembered that over the long period the values of all existing buildings having a useful life still remaining are affected by changes in the cost of replacing them. All other factors being equal, if the cost of building a building doubles, the value of all useful existing buildings of the same type would tend to take on a part of the rise. It now seems almost certain that the cost of building buildings in the future will be higher than their present costs, although the chances are that during the first six months of the year there may not be very rapid increases due to the fact that some of the materials which go into buildings will be more plentiful because of the restricted amount of building being done. Over the next few years, however, it will be quite surprising if the cost of building does not increase by a considerable percentage.

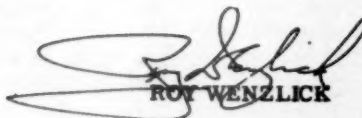
Another factor which will tend to increase real estate values on existing buildings will be the limitations on construction which necessarily follow and accompany an intensive war effort. Residential building during 1951 will shrink by from 30 to 40%. This means that the volume of building which we were doing during 1950 and which, if continued, would inevitably have resulted in a housing surplus in a relatively short time, will now no longer threaten the existing housing supply. The balanced condition in most communities of supply and demand for housing will continue, with the probability that in many areas where intense defense activities take place a housing shortage will again develop with the scarcity premium which a housing shortage always brings in the price of real estate.

Because of many of the uncertain conditions existing today we would not advise,

as we did in the late thirties, the purchase of slim equities in real estate, but would now advise the purchase of substantial equities or, better still, the outright ownership of real estate owned free and clear. A person with a substantial equity in real estate or a person that owns it free and clear will, we believe, be able to ride through the period ahead with the maximum conservation of his principal. The speculator, of course, can make more money by buying slim equities in a rising market, but due to the fact that so much of our real estate boom is already behind us, we feel that this sort of a policy involves risks greater than the average individual would care to run.

I feel that it would be a mistake to end this bulletin without one word of caution on a possibility which might reverse all inflationary trends and bring about a period of deflation. To me, the only possibility of a sudden reversal of the trend would be a revolution in Russia. Should a revolution of this sort start, it would make all of our defense activity unnecessary and would also bring about a reduction in armament throughout the world. We would cancel in a very short time our plans for additional armament, and as government contracts were canceled a period of contraction in general business would start. It may be that this would bring the depression which would ordinarily follow a period of inflation such as the one we have just been through.

Certainly, I would not say that this is a probability, but I still think that it is a possibility and should, therefore, be taken into consideration by the investor at the present time. That is an additional reason why I believe that slim equities are not advisable.



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